

ST 02-7

Tax Type: Sales Tax

Issue: Enterprise Zone (Exemptions)

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
SPRINGFIELD, ILLINOIS**

**“EMPIRICAL DEVELOPMENT
CORPORATION”,**

Taxpayer

v.

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

**No. 96-ST-0000
IBT 0000-0000**

**Barbara Rowe
Administrative Law Judge**

RECOMMENDATION FOR DISPOSITION

Appearances: Daniel Davlantis of Scott and Scott, P.C. on behalf of "Empirical Development Corporation"; Special Assistant Attorney General Charles Hickman on behalf of the Illinois Department of Revenue.

Synopsis:

This matter involves a Notice of Tentative Denial of a Claim for credit or refund of Retailers' Occupation Tax and Use Tax paid for the period of August 1992 through December 1994 in the amount of \$46,401.00. The claim is in part for a refund of taxes paid pursuant to an audit on materials, bought by "Empirical Development Corporation" (hereinafter referred to as the "Taxpayer" or "Empirical"), in connection with a construction project in an enterprise zone. The basis of the denial by the Illinois Department of Revenue (hereinafter referred to as the "Department") is that the taxpayer has not established that the tax was not paid in error or that unjust enrichment would not result if the claim were paid. The taxpayer timely protested the notice. An evidentiary hearing was held during which the taxpayer argued that that the taxpayer

satisfied the requirement that it be a retailer located (or maintain its place of business) within the municipality that established the enterprise zone in question. After a thorough review of the facts and law presented, it is my recommendation that the refund claim be granted in part. In support thereof, I make the following findings and conclusions in accordance with the requirements of Section 100/10-50 of the Administrative Procedure Act (5 ILCS 100/10-50).

FINDINGS OF FACT:

1. The *prima facie* case of the Department was established by the admission into evidence of the Notice of Tentative Denial of Claim and related documents. (Dept. Ex. Nos. 1-12; Tr. p. 50)

2. On March 6, 1996, the Department issued the taxpayer a Notice of Tentative Denial of Claim for Retailers' Occupation Tax (hereinafter referred to as "ROT") and Use Tax (hereinafter referred to as "UT") for the period of August 1992 through December 1994. The Department's Notice of Denial shows taxpayer's address (Address #1) Springfield, Illinois. (Dept. Ex. No. 1)

3. The Department conducted an audit of the taxpayer for the period of August 1992 through December 1994 and established a liability of \$46,401.00. The Audit Correction and/or Determination of Tax due is dated November 7, 1995. The taxpayer paid the tax due and then filed a claim against the audit. (Dept. Ex. No. 2; Tr. pp. 12-13)

4. The liability is for materials, office furniture, a tractor, and traffic control materials for which the taxpayer did not charge use tax to its customers or pay use tax to its vendors. (Dept. Ex. Nos. 3 & 4)

5. The sole basis for the assessment regarding the materials is that the taxpayer was not located in the enterprise zone in the City of Springfield. (Dept. Ex. Nos. 1-4; Tr. pp. 14-16, 30, 42-43)

6. The ROT audit detail lists taxable exceptions for six sales of tangible personal property "Empirical" made to "ABC Partners, Inc." (hereinafter referred to as "ABC") and one sale to "Empirical Center, Inc." (Dept. Ex. No. 4)

7. The UT detail lists three purchases “Empirical” made from “Peters & Sons Lumber” for materials¹, one for materials from “ABC”², one from “Mr. Roger’s Interiors” for office furniture³, one from “Harper Valley, Inc.” for a tractor, one from “Empirical Center, Inc.” for materials⁴, and one from “PSU Corp.” for traffic control materials⁵. (Dept. Ex. No. 4)

8. The taxpayer agrees with the assessment for tax due on the tractor. (Tr. p. 90)

9. The Illinois Business Registration NUC-1, dated June 2, 1992, shows the business address of the taxpayer as (Address #2) Springfield, Illinois. (Address #2) is in the corporate limits of the Village of Sherman, Illinois and not in the Springfield enterprise zone. The NUC-1 also has a question at No. 7 as to whether the business is located either inside the city, village, or town, or outside those locations. The taxpayer checked the line on the form indicating that the business was located inside the City of Springfield. The home addresses of the two owners/officers of the taxpayer, “Dave” and “Don Peters”, according to the NUC-1 is also (Address #2), Springfield, Illinois. Sherman, Illinois is a suburb of Springfield, Illinois. (Dept. Ex. No. 5; Tr. pp. 18-20, 34)

10. The Small Business Corporation Replacement Tax returns and ST-1 Sales and UT returns filed by the taxpayer for the periods in question show the taxpayer's address as (Address #2), Springfield, Illinois. (Dept. Ex. Nos. 6-9; Tr. pp. 21-23)

11. The Articles of Incorporation of the taxpayer, dated December 11, 1991, list the initial registered office at (Address #2), Springfield, Illinois. (Dept. Ex. No. 9; Tr. pp. 23-24)

¹ The taxpayer has not established how it used the materials purchased from “Peters & Sons Lumber” in the enterprise zone. In addition, “Peters & Sons Lumber” is in Sherman, Illinois and not within a county or municipality which has established the Enterprise Zone at issue. Therefore, the imposition of this tax is upheld.

² The taxpayer has not established what type of materials were purchased from “ABC” or how they were incorporated into real estate located in the enterprise zone. “ABC” was formed to construct the hotel, not act as a retailer to the taxpayer. The taxpayer has failed to establish how this transaction qualifies for the exemption. Therefore, the imposition of this tax is upheld.

³ As this transaction is not for building materials incorporated into real estate and as the parties did not address the transaction, the tax is upheld.

⁴ The taxpayer has not established what type of materials were purchased from “Empirical Center” or how they were incorporated or used by the taxpayer in the enterprise zone. Therefore, the imposition of this tax is upheld.

⁵ As this transaction is not for building materials incorporated into real estate and as the parties did not address the transaction, the tax is upheld.

12. The sales tax audit payment checks, dated August 24, 1995, list the address of the taxpayer as (Address #2), Springfield, Illinois. (Dept. Ex. Nos. 10 & 11; Tr. pp. 24-26)

13. In mid-1995, the Department's records showed (Address #3) Springfield, Illinois as the taxpayer's address. Shortly after the audit of the taxpayer, the Department was notified of the (Address #3) address and verified it. (Tr. pp. 20-21, 34-35)

14. The taxpayer was formed to be a retailer of building materials purchased for physical incorporation into an enterprise zone. The Department's auditor determined that "the taxpayer also consumed tangible personal property as a construction contractor by transferring the property to others as part of a contract." (Tr. pp. 16, 52, 60)

15. On March 23, 1992, "Dave Peters", taxpayer's president, quitclaimed a 103 acre tract of land to the taxpayer. The address of the taxpayer on the deed is (Address #2) Springfield, Illinois. (Dept. Ex. Nos. 5 & 12; Respondent's Ex. No. 7; Tr. pp. 15-16, 26, 38)

16. In consideration for the land, the taxpayer issued 975 shares of stock to "Dave Peters" and 25 shares to "Don Peters". (Respondent's Ex. No. 2; Tr. pp. 53-54)

17. When "Dave Peters" purchased the land in 1991 it was a farm. There was no physical building on the land. (Tr. pp. 51-53)

18. The then mayor of the City of Springfield approached "Peters" about developing the north side of the city and using the 103 acres to do so. "Peters" met with a representative of the Department of Commerce and Community Affairs and the mayor to discuss the construction and the availability of the tax exemption. On June 19, 1992, Springfield City Ordinance No. 00000 was amended placing the 103 acre property in the enterprise zone. (Respondent's Ex. Nos. 6 & 7; Tr. pp. 52-55, 84-87)

19. The surveyor's certificate stating that the property was sub-divided into 13 lots and streets by iron reinforcement rods identifying the lot corners on the plat was recorded on January 4, 1993, in Sangamon County. The name of the subdivision is "Empirical Plaza". A [m]otel was the first building planned for in the subdivision. It was built on lot ? of the subdivision. (Respondent's Ex. No. 8; Tr. pp. 26, 56)

20. The taxpayer, although a separate legal entity, has ties with “Peters & Sons, Lumber”, “ABC”, and “Empirical Center”. The auditor conducted the complete audit of the taxpayer from “Peters & Sons Lumber” at (Address #2), Sherman, Illinois. (Dept. Ex. No. 2; Tr. pp. 6, 29-31, 59)

21. In the early 1990's “Dave Peters”, “John Doe”, and “Richard Roe” formed “ABC” to construct a hotel on the property and purchase materials from the taxpayer. Letters dated July 16, 1992 gave notification of this fact to the taxpayer and “Peters & Sons Lumber Company”. “ABC” addressed its letter to the taxpayer to (Address #4), Springfield, Illinois. The address of the taxpayer was (Address #4) on the letter sent to “Peters & Sons Lumber Company. (Respondent's Ex. Nos. 9 & 10; Tr. pp. 62-63)

22. The 0000 block number is about in the center of the 103 acres and (“A” street) runs parallel to the subject property. (“A” street) is not located on the 103 acres. Rather, (“A” street) runs along the west side of the property in question. (Respondent's Ex. Nos. 8, 13-15)

23. On June 17, 1992, “ABC” obtained a building permit from the Building and Zoning Department of the City of Springfield, Illinois for a new [motel] in the enterprise zone. The Building and Zoning Department of the City of Springfield, Illinois on [date] 1993, issued the Certificate of Occupancy. (Respondent's Ex. Nos. 11 & 17)

24. The construction of the hotel began after “ABC” obtained the building permit. Problems were encountered because a state highway runs along the [designated] side of the property and the State could not decide where the entrance to the property should be placed. An engineer moved the planned entrance about five times. The street entrance to the hotel was completed at about the same time as the hotel was completed. (Tr. pp. 57-58)

25. The post office would not allow the taxpayer to erect a mailbox on the 103 acre property because there were no streets. The utility company would not run telephone lines to the “Empirical Plaza” location because there were no streets. (Tr. pp. 58-60)

26. A trailer was on the property at lot ##. The trailer contained a desk and a file cabinet. A sign on the outside of the trailer identified it as belonging to the taxpayer. The

taxpayer used portable telephones. When the [m]otel was partially completed, the taxpayer moved its operations into the building, because it was heated and the trailer was not. (Tr. pp. 60-62, 73-76)

27. The Department's auditor inquired whether the taxpayer had a physical location at the work site. She was told that a work trailer was there during the construction of the hotel. (Tr. pp. 26-27)

28. Among the taxpayer's books and records, the auditor found a letter from "ABC" to the taxpayer dated July 16, 1992, stating "'ABC" is currently constructing a motel on the property located at (Address #4). which is within an Enterprise Zone. All invoices or supplies will be no tax as we are within the Enterprise Zone.'" (Respondent's Ex. No. 9; Tr. p. 42)

29. The taxpayer sent a letter to "Peters & Sons Lumber Company" on July 16, 1992 stating "We are currently supplying material for Springfield [motel] located at (Address #4). which is located within an Enterprise Zone and all material will be billed out no tax. Please adjust our account to reflect the fact it is NO TAX/ENTERPRISE ZONE." (Respondent's Ex. No. 10)

29. The invoices from the taxpayer to "ABC" for the time period in question show the address of the taxpayer as (Address #4), Springfield, Illinois. The taxpayer needed this address on the forms to direct the delivery of the materials. (Respondent's Ex. Nos. 13-15; Tr. pp. 66-68)

30. The bills from "Peters & Sons Lumber" to the taxpayer for November 1992 and December 1992 show the address of (Address #5), Springfield, Illinois. This was the location of the job trailer at that time. (Respondent's Ex. Nos. 14 & 15; Tr. pp. 95-96)

31. The streets on the subject property, currently named "Empirical" and "Peters" Drives, were in place about 30 days before the [m]otel opened. (Respondent's Ex. Nos. 8 & 18; Tr. p. 68)

32. The taxpayer operated with its "floating checkbook" that would be carried from location to location. (Tr. pp. 97-106)

33. The taxpayer's bookkeeper wrote 99% of the checks and invoices from her desk at (Address #2), Springfield, Illinois. (Tr. pp. 97-106)

34. Located at (Address #2), Sherman, Illinois is "Peters & Sons Lumber". It is not a location in an enterprise zone. (Tr. pp. 18-20, 50-51, 84)

35. "Peters & Sons Lumber" has been in business for xx years. It is the principle business for "Dave Peters". "Dave Peters" is also a shareholder and registered agent of the taxpayer, and a partner in "ABC". "Peters & Sons Lumber" would sell material to the taxpayer and the taxpayer would sell to "ABC". (Tr. pp. 61-65)

36. The carpenters employed in the construction of the hotel were in and out of the job trailer located on lot xx. They would contact "Dave Peters" at the trailer with an order for lumber. He would contact "Peters & sons Lumber" and place the order with the bookkeeper. She would write an invoice and have the materials shipped to the enterprise zone location. (Tr. pp. 61-65)

37. At the end of November or early December 1992, the taxpayer moved its operations from the trailer to the [m]otel when the hotel was sufficiently completed and the weather turned cold. (Tr. pp. 73-74)

38. The auditor was told at the start of the audit that there was no mail service or mail delivery to the "Empirical Development" property. (Tr. p. 36)

39. The auditor made no physical inspection to ascertain if the taxpayer had an office or suite in the hotel. The auditor checked the Department's records, and these records did not show a location for the taxpayer at the hotel. The auditor also attempted to call the taxpayer at a hotel suite and was referred to "Peters & Sons Lumber". The auditor was not aware of any office used by the taxpayer in the hotel. (Tr. pp. 29, 38-44, 79)

40. The auditor never saw evidence of a work trailer. (Tr. p. 27)

41. In 1994, the auditor performed the audit of "ABC" at the (Location). The (Location) is the former [motel] that was built and is owned by "ABC" on the 103 acre property. The [m]otel was completed in 1993. (Tr. pp. 38-44, 67, 79)

42. At the time of the hearing a [several businesses were located on the property] (Tr. pp. 75-82, 91)

43. The taxpayer built a stand-alone facility in the “Empirical Plaza” for its operations sometime in either 1994 or 1995. (Tr. p. 80)

CONCLUSIONS OF LAW:

The Retailers' Occupation Tax Act imposes a tax on retailers in the State of Illinois pursuant to 35 **ILCS** 120/2:

Tax imposed. A tax is imposed upon persons engaged in the business of selling at retail personal property...

The Use Tax Act similarly imposes a tax on persons using tangible personal property in the State of Illinois. 35 **ILCS** 105/3. The Acts also have exemptions from the tax. The exemption provision at issue regards Enterprise Zones, which for the years at issue provided in relevant part:

Each retailer whose place of business is within a county or municipality which has established an Enterprise Zone pursuant to the Illinois Enterprise Zone Act and who makes a sale of building materials to be incorporated into real estate in such enterprise zone by remodeling, rehabilitation or new construction, may deduct receipts from such sales when calculating the tax imposed by this Act. 35 **ILCS** 120/5k; 35 **ILCS** 105/3-65 (incorporating ROT non-taxability to the UT by reference.)

It is well settled in Illinois that when a statute purports to grant an exemption from taxation, the tax exemption provision is to be construed strictly against the one who asserts the claim of exemption. Thomas M. Madden and Co. v. Department of Revenue, 272 Ill.App.3d 212 (2nd Dist. 1995). Whenever doubt arises, it is to be resolved against exemption and in favor of taxation. Follett's Illinois Book & Supply Store, Inc. v. Issacs, 27 Ill.2d 600 (1963). A claimant must prove clearly and conclusively its entitlement to an exemption. Wyndemere Retirement Community v. Department of Revenue, 274 Ill.App.3d 455 (2nd Dist. 1995) *leave to appeal denied* (164 Ill.2d 585). Further, in ascertaining whether or not a property is statutorily tax

exempt, the burden of establishing the right to the exemption is on the one who claims the exemption. Midway Airlines, Inc. v. Department of Revenue, 234 Ill.App.3d 866 (1st Dist. 1992) *leave to appeal denied* (146 Ill.2d 632)

Under the certificate of the Director, the Department admitted into evidence the Notice of Tentative Determination of Claim and related documents. Section 6b of the ROT Act provides that the notice issued by the Department is *prima facie* correct. 35 ILCS 120/6b. Once the Department establishes its *prima facie* case by submitting the document into evidence, the burden shifts to the taxpayer to overcome this presumption of validity. Clark Oil & Refining Corp. v. Johnson, 154 Ill.App.3d 773, 783 (1st Dist. 1987) *leave to appeal denied* (116 Ill.2d 549). To prove its case, a taxpayer must present more than its testimony denying the Department's assessment. Sprague v. Johnson, 195 Ill.App.3d 798, 804 (4th Dist. 1990) *leave to appeal denied* (133 Ill.2d 573) The taxpayer must present sufficient documentary evidence to support its claim for exemption. *Id.*

The Illinois Enterprise Zone Act was enacted by P. A. 82-1019, effective December 7, 1982, "to explore ways and means of stimulating business and industrial growth and retention in depressed areas and stimulating neighborhood revitalization of depressed areas of the State by means of relaxed government controls and tax incentives in those areas." 20 ILCS 655/2. P.A. 82-1019 also amended the Retailers' Occupation Tax Act by adding section 5k.

The regulations issued by the Department, as they were in effect for the tax periods, set forth record keeping requirements for retailers located in municipalities or counties that have established enterprise zones and who are selling building materials for incorporation into real estate being rehabilitated, remodeled or constructed in those zones. 86 Admin. Code ch. I, § 130.1951 states:

- a) Building Materials Purchased for Physical Incorporation into Real Estate Located in an Enterprise Zone
 - 1) Effective September 1, 1985, a deduction from Illinois Retailers' Occupation Tax liability exists for gross receipts from retail sales of building materials which will be incorporated into real estate

located in an *enterprise zone by remodeling, rehabilitation or new construction*. (Section 5k of the Act)

- 2) The retailer of qualifying building materials must be located in the municipality or in the unincorporated area of the county which has established the enterprise zone into which the building materials will be incorporated. In order to establish that the retailer is located in the municipality or unincorporated area of the county which has established the enterprise zone, the retailer must at the time of sale:
 - A) have an identifiable physical presence in the municipality or the unincorporated area of the county that has established the enterprise zone;
 - B) be registered with the Department as a retailer at a location in the municipality or in the unincorporated area of the county that has established the enterprise zone; and
 - C) be able to document the acceptance of purchase orders at a location in the municipality or the unincorporated area of the county that has established the enterprise zone.
- 3) In order to establish that the purchaser purchased qualifying building materials from a qualified retailer, the following two separate transactions must exist:
 - A) a sale from a supplier to the retailer who is located in the jurisdiction that created the enterprise zone (exempt as sales for resale); and
 - B) a sale from the retailer who is located in the jurisdiction that created the enterprise zone to the purchaser (exempt by reason of the enterprise zone building materials exemption).

The issue in this matter is whether the taxpayer established a bona fide place of business in the Springfield enterprise zone during the tax period at issue.

In the case at bar, “Peters & Sons Lumber” is the supplier, and the taxpayer is the retailer selling building materials to “ABC” who incorporates those materials into real property incorporated in an enterprise zone.

Initially the taxpayer contends that the application of collateral estoppel is appropriate herein regarding the exemption for the purchases at issue. In support of its argument, taxpayer relies on xxxx v. xxxx, which the taxpayer appended to its final brief. Xxxx v. xxxx is a decision

by the 4th District Appellate Court pursuant to S. Ct. Rule 23 [and therefore may not be cited as precedent]

As the taxpayer accurately notes, estoppel requires that the party to be bound must have actually litigated the particular issue in a prior adjudication. However, the issue of whether the taxpayer in this matter was located within the municipality that established the enterprise zone was not litigated in the case relied upon by the taxpayer nor was the taxpayer a named litigant in the case. Because that issue was not raised in the prior proceeding, estoppel is not appropriate here.

The Department asserts that the taxpayer did not establish a bona fide place of business in the Springfield enterprise zone because the auditor never saw the trailer that the taxpayer states was located in the enterprise zone and from which the taxpayer conducted some of its business. The Department cites the following factors as evidence of its position: that taxpayer had no mail delivered to the “Empirical Plaza” location, the alleged trailer was not staffed on a regular basis, the taxpayer had no telephone at that location, and the taxpayer failed to conduct regular business operations at that location. In fact, according to the Department, the auditor had no knowledge of taxpayer’s operation in the Springfield enterprise zone and no knowledge of the trailer on the premises.

Neither the statute nor the regulations applicable to the tax periods address the question of what constitutes having a “place of business” within a municipality or an unincorporated area of a county which has established an enterprise zone. There is no definition of “retailer” nor are there any provisions that prescribe how much substance needs to be put in a corporation established by a contractor to act as a retailer in a municipality or an unincorporated area of a county which has established an enterprise zone.

Although the “Empirical Plaza” location in Springfield was registered for the taxpayer with the Department in 1995, after the audit period, there is no question that the taxpayer owned the property during the audit period in question. The taxpayer called two witnesses at the hearing both of whom credibly testified that the taxpayer had a trailer on the property and conducted its business at the trailer during the time period in question. When the weather turned too cold, the [m]otel was sufficiently completed that the taxpayer moved its business location to the hotel. Business could be completed from there. There was a sign on the trailer identifying that it was the location of the taxpayer. That testimony was not controverted.

Although the majority of the purchase orders, invoices, and checks for the enterprise zone projects were processed at (Address #2), Sherman, Illinois neither the statute nor the regulations quantifies the amounts of business that must be carried on in the place of business. All that is required is that the taxpayer establish a place of business within the county that has established the enterprise zone. The hotel was completed in just over a year in the enterprise zone. It is obvious that lumber was delivered in the enterprise zone to erect the hotel.

In support of its position that the taxpayer had no bona fide presence in the enterprise zone, the Department relies upon Department of Revenue v. Build 'em Up Supply Company (Dept. of Revenue Administrative Hearing Decision #ST 99-8). Build 'em Up Supply Company involves the issue of whether Build 'em Up Supply Company established retail establishments in two Illinois enterprise zone locations. The locations were not staffed on a regular basis, no telephones were located there, no rent or utilities were paid, and regular business hours were not kept. The taxpayer in Build 'em Up did keep desks, chairs, file cabinets, a lap top computer, and calculator at office spaces in the enterprise zone and checks, purchase orders, and invoices were processed at those locations as necessary. Build 'em Up recognized the presence of the taxpayer

in the two enterprise zones at issue in that case based upon the records kept. The administrative law judge found that the taxpayer was entitled to the credit memoranda based upon the taxpayer having a place of business in the enterprise zone.

From Build 'em Up Supply, the Department argues that the registration of the taxpayer for the Department's purposes at the Sherman, Illinois address rather than an in-zone location and the payment of 99% of the bills at the Sherman location are the two critical facts that mandate a finding against the taxpayer in this matter. I do not agree. The credible testimony of the taxpayer's two witnesses coupled with the exhibits establishing the lack of roads and access for the post office and utility companies explains why the taxpayer used (Address #2), Springfield, Illinois for its registration address. As the taxpayer correctly notes in its post-hearing brief, (p. 8) a registered address is not the same as a place of business. I find that this taxpayer established its place of business in the enterprise zone during the time period in question.

There is nothing in the statute that prevents a taxpayer from arranging its affairs to minimize taxes. See First Chicago Building Corp. v. Department of Revenue, 49 Ill.App.3d 237 (1st Dist. 1977). That is what the taxpayer did in this case. Taxpayer's creation and function were consistent with the legislative intent in enacting the Illinois Enterprise Zone Act. Craftmasters v. Department of Revenue, 269 Ill.App.3d 934 (4th Dist. 1995) *leave to appeal denied* (162 Ill.2d 565). For all of the reasons stated above, I conclude that the testimony and evidence of record submitted by the taxpayer regarding the issue of whether the taxpayer established a bona fide presence in the enterprise zone is sufficient to overcome the Department's *prima facie* case on that issue.

Therefore, I recommend that the taxpayer's claim regarding the building materials purchased to be incorporated into real estate located in the enterprise zone be allowed in part. As

the parties did not address the UT transactions including the materials, office furniture and traffic control materials, and the taxpayer admitted tax is due on the purchase of the tractor, the tax corresponding to that portion of the claim is denied.

Respectfully Submitted:

January 9, 2002

Barbara S. Rowe
Administrative Law Judge